An Roinn Airgeadais
Department of Finance

Contingent Liabilities: an overview

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Rounding may affect totals throughout this document.

Executive Summary

A comprehensive budgetary framework includes a complete evaluation of financial obligations – both contingent and realised. On this basis, the recording and monitoring of both contingent and off-balance sheet liabilities is essential for a prudent fiscal sustainability analysis.

Contingent liabilities of government represent money the government may owe if a specified event, upon which they are contingent, occurs.

Policy instruments, such as government guarantees, which result in contingent liabilities, can assist in the achievement of policy objectives while having a limited impact on the government's financial position. Through such policy tools, the government can promote economic activity, restore stability and promote investment in public infrastructure while keeping the impact on the fiscal position and government balance sheet to a minimum.

Although policies that give rise to contingent liabilities may be successful at facilitating government objectives, they do create a potential risk for the long-term financial sustainability of the government. During the global financial crisis, the level of government guarantees relating to financial sector liabilities sharply increased across Europe emphasising a need for comprehensive reporting of contingent liabilities. Consequently, the enhanced economic governance – the so-called 'six-pack' – put in place across the European Union requires detailed reporting of contingent liabilities of government with potentially large impacts on public budgets. This paper aims to supplement this reporting requirement with an analysis of the trend in these contingent liabilities over time and in comparison to EU Member States, as well as extending the scope to other off-balance sheet liabilities.

Contingent liabilities have fallen sharply from a high of 157.3 per cent of GNI* in 2013 to 68 per cent of GNI* in 2019 with Ireland comparing favourably by EU standards, trending at or below the EU norm.

The Covid-19 pandemic, which once may have been considered an implicit liability, has transpired into both explicit direct and contingent liabilities for governments across the world. In the case of Ireland, the policy response focuses predominantly on direct income supports for households, businesses and the health sector. The introduction of public restrictions and the increase in expenditure by government, with an aim of protecting public health while cushioning the financial impact on society, has resulted in an increase in general government debt through an increase in direct explicit liabilities. Explicit contingent liabilities also increased in the form of government guarantees extended to initiatives introduced nationally and internationally in response to the crisis. On this basis, the values of contingent liabilities for end-2020 are likely to increase in both Ireland and across the EU Member States, further highlighting the importance of reporting and monitoring such items.

Section 1: Introduction

Contingent liabilities are agreements whereby one party, in this case the Government, is obliged to provide payment or a series of payments to another party, only if certain specific conditions materialise. Contingent liabilities do not feature on the balance sheet of the government: instead, these are *potential* liabilities of government and only become *actual* liabilities of government if those conditions, upon which they are contingent, materialise.

While not directly included on the government's balance sheet, the recording and monitoring of contingent liabilities is important for budgetary analysis and in the formulation of policy, *inter alia* as high levels of contingent liabilities may present undesirable risks to the government's balance sheet.

A comprehensive budgetary framework is composed of several elements, one of which is the availability of transparent, accurate information regarding contingent liabilities of the government. The global financial crisis 2008-2010 (GFC), where the policy response in many advanced countries involved large-scale government guarantees of financial sector liabilities, emphasised the need for comprehensive, real-time information regarding contingent liabilities.

The enhanced economic governance – the so-called 'six-pack' – put in place in the European Union following the GFC and the subsequent euro area sovereign debt crisis, sets common standards and practices for member states in relation to fiscal reporting. In particular, the obligations set out in Council Directive 2011/85 of 8th November 2011 require the publication of data on contingent liabilities of government with potentially large impacts on public budgets.[1] These include "*government guarantees, non-performing loans, and liabilities stemming from the operation of public corporations*". Member states are also required to publish information on "*the participation of general government in the capital of private and public corporations*". Member states are required to publish these data, and to report to *Eurostat* (the EU's statistical agency), which subsequently publishes data for all member states.[2] In Ireland, data on contingent liabilities are published annually by the *Department of Finance*[3], and transmitted to *Eurostat* by the *Central Statistics Office* (CSO).

The purpose of this document is to supplement the data published by the Department. In section 2, the various concepts relating to government liabilities are explained, the evolution of the data over time and in comparison to member states is examined and an insight into other *potential* liabilities facing the government, beyond what is required to be reported, is documented. Section 3 concludes.

Section 2: Contingent liability by category

A prudent budgetary policy includes an overview of all financial obligations facing the State – this paper aims to support this by looking at *potential* liabilities that, while unlikely, may pose a financial cost to the State.

This section presents Ireland's level of contingent liabilities and non-performing loans, as required under Council Directive 2011/85 of 8th November 2011 – it examines their evolution over time and in comparison to other EU Member States. Box 1 provides a description of the different types of liabilities, while Box 2 and Box 3 extend the analysis, beyond the reporting requirements, to include additional *potential* liabilities facing the government.

2.1: Government guarantees

In many countries, the government may provide guarantees, partially or fully covering the borrowing of an entity, contingent on the occurrence of a clearly specified uncertain event. Government guarantees, extended to bodies outside the general government sector, are a contingent liability.

[1] https://eur-lex.europa.eu/LexUriServ/LexUriServ.do?uri=OJ:L:2011:306:0041:0047:EN:PDF
[2] https://ec.europa.eu/eurostat/web/products-eurostat-news/-/ddn-20210129-1?redirect=%2Feurostat%2Fweb%2Fmain%2Fnews%2Fwhats-new
[3] https://www.gov.ie/en/collection/262006-contingent-liabilities-update/

Box 1: Types of liabilities

Liabilities facing the government include *direct liabilities* and *contingent liabilities*, both of which can be *explicit* or *implicit*. See figure A.1 in the Annex for a visual representation.

Explicit liabilities are specific government commitments defined by contract or law, in which the government face a legal obligation to settle the liabilities as they fall due.

Implicit liabilities represent a moral obligation or expected responsibility of the government, which while not legally binding, have the potential to generate financial demands for the government due to public expectation and/or political pressure. These liabilities are usually only recognised after an event occurs, and by their nature are uncertain and harder to quantify

Government *explicit direct liabilities* are monies that the government has an obligation to pay. Perhaps the most commonly understood example is a sovereign debt instrument – a bond or a bill – typically issued by a debt management office (the National Treasury Management Agency in Ireland's case) on behalf of the government. When issued (and sold), the government promises to repay the face value of the instrument at a specified date in the future. In the case of this liability, the financial obligation is recognised on the government balance sheet when the liability agreement is initiated.

Direct implicit liabilities are generally considered as longer-term presumed consequences of public expenditure policies, which are not captured on the government's balance sheet. In countries, that have pay-as-you-go pension schemes, future pension-expenditure demands are an example of such a liability facing the government.

In comparison, *contingent liabilities* are amounts the government *may* owe, but the value, timing or even existence of the obligation will depend on the occurrence of an uncertain future event. Contingent liabilities are not recognised on the balance sheet of the government unless the uncertain event occurs; only then will the government's obligation be called upon and the outstanding value of the liability at that time recognised and added to the balance sheet.

A simple example of a transaction that would give rise to an *explicit contingent liability* involves a government loan guarantee granted to an enterprise (say a small - or medium-sized enterprise, SME). In this example, three parties are involved: the lender (bank), the borrower (SME) and the guarantor (government). The bank provides a loan to the SME based on an agreement that in a scenario where the SME cannot make repayments the government will step in to take over the SMEs obligations to the bank. In this case, the bank records a loan asset, the borrower records a loan liability and the government records a contingent liability. The government's obligation to repay the loan is conditional on the SME defaulting, so the existence and value of the liability for the government is dependent on a particular event occurring and therefore will only be recognised as a liability on the government's balance sheet, if such a scenario becomes reality.

Contingent implicit liabilities are unknown, until a failure occurs. The triggering event, the level of risk and the value of the *potential* obligation the government may face are all uncertain. *Contingent implicit liabilities* arise from a government's commitment to maintain stability, such as an unrecognised perceived responsibility to ensure stability within a country's financial system.

Government guarantees come in many shapes and sizes. One of the most common forms involves a loan guarantee that a government may extend to an enterprise. Other forms of guarantees include trade and exchange rate guarantees; income, profit, and rate of return guarantees; and minimum pension guarantees.

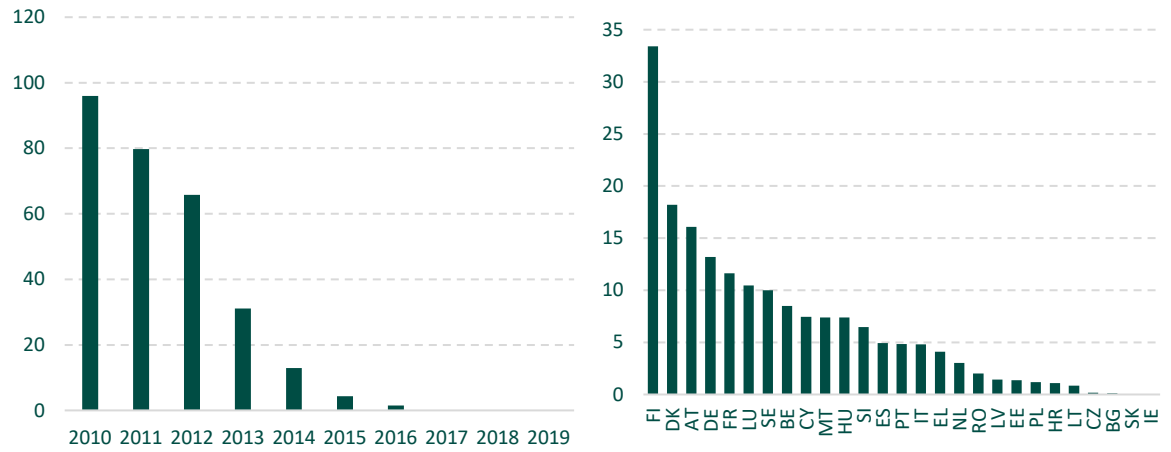
The objective of this type of policy intervention is to improve the perceived credit rating of the enterprise (or sector): enabling the partner enterprise to source market-based finance at a lower cost than would otherwise be the case. In this way, the government can promote economic activity without a direct impact on its own balance sheet. That said, the risk to the loan originator (such as a bank) of the enterprise defaulting on its obligations is simply transferred to the government; if sufficiently large, lenders to the government will demand a risk premium in order to compensate for this risk of lending to a sovereign issuer.

Data on Ireland's government guarantees are transmitted to *Eurostat* as part of the bi-annual Excessive Deficit Procedure (EDP) notification, and are published by the CSO in conjunction with its *Government*

Finance Statistics publication.[4] The values reported for government guarantees are consolidated, including only guarantees provided to units classified outside the general government sector. These data exclude any government guarantees that are recognised on the general government's balance sheet, guarantees issued within the guarantee mechanism under the Framework Agreement of the European Financial Stability Facility (EFSF), derivative-type guarantees, deposit insurance guarantees, and guarantees issued regarding events whose occurrence is difficult to cover via commercial insurance (natural disasters). Box 2 contains a more inclusive list of guarantees granted by the Irish government.

Figure 1a shows the evolution of the stock of Irish government guarantees over the last decade. It illustrates the fall in the prominence of guarantees issued by the State since 2010. In the aftermath of the financial crisis, government guarantees played a vital role in restoring stability and trust in the Irish financial system through guarantees on liabilities of key financial institutions and guarantees for the borrowing of the *National Asset Management Agency* (NAMA).

Figure 1: Government guarantees a) Ireland; b) EU Member States 2019, per cent of GDP



Note: The UK is included in the graph as the data represents 2019 positions.
Underlying Irish data is provided in annex, table A.1.
Source: CSO and Eurostat.

The *Credit Institutions (Financial Support) Scheme* ("CIFS") which commenced on the 30th September 2008, provided a government guarantee for all deposits (retail, commercial, institutional and inter-bank), covered bonds, senior debt and dated subordinated debt (lower tier II) for seven, systemically important, Irish credit institutions, before expiring on 29th September 2010. The Credit Institutions (Eligible Liabilities) Guarantee Scheme ("ELG Scheme") effectively superseded it on the 9th December 2009. The ELG Scheme restricted eligible liabilities to deposits and senior unsecured debt only, with the issuance period for eligible liabilities ending on the 28th March 2013. Eligible liabilities covered under the Scheme, incurred up to that time, continued to be covered up to their maturity date, which could be up to five years from the date the liability was incurred. As such, guaranteed liabilities declined over the period March 2013 to March 2018.

An additional driver in the downward trend seen in figure 1a was the redemption of government guaranteed NAMA debt. NAMA was established in 2009 to remove problematic land and development loans from participating banks balance sheets, ultimately acquiring loans worth €26.2bn from the banks for consideration of €31.8bn. The consideration of €31.8bn was paid to the banks in the form of €30.2bn ECB eligible, government guaranteed senior bonds (a contingent liability for the State) and €1.6bn unguaranteed subordinated bonds.[5] As NAMA redeemed these bonds the level of associated contingent liabilities of the government decreased, with a full redemption and extinguishing of associated government guarantees by end-2017.

[4] https://www.cso.ie/en/statistics/governmentaccounts/governmentfinancestatisticsa/
[5] Further information on NAMA is available: https://www.gov.ie/en/publication/2f5f9e-national-asset-management-agency-nama/

At end-2019, Ireland's government guarantees amounted to just 0.002 percent of GDP, a figure that was minor in a European context (figure 1b). Across the European Union, government guarantees are more prominent in member states such as Finland (33.4 per cent of GDP), Denmark (18.2 per cent of GDP), Austria (16.1 per cent of GDP), Germany (13.2 per cent of GDP) and France (11.6 per cent of GDP).

Finally, it is worth pointing out that guarantees have been an integral part of the policy response to the Covid-19 pandemic, both in Ireland and across the EU. Once published the data for 2020 will likely show an increase in these contingent liabilities. This is discussed further in Section 2.5.

Box 2: Government guarantees reported in Finance Accounts 2019

Table 1 presents guarantees provided by the State, under specific legislation, for the due payments on outstanding liabilities. These guarantees are reported in statement 1.11 of the Finance Accounts. At year end-2019, Ireland's level of guaranteed liabilities was €5.0bn or 2.3 per cent of GNI* (1.4 per cent of GDP) – with the Housing Finance Agency availing of the largest guarantee at near €4.5bn.

The level of government guarantees outlined in Section 2.1 is much smaller than the values outlined here – this is a result of consolidation, as guarantees extended to government bodies are excluded in the reporting in section 2.1. The Strategic Banking Corporation of Ireland and the Housing Finance Agency are both bodies within the general government, therefore, their liabilities, including those subject to government guarantee, are included on the general government balance sheet.

Table 1: Guaranteed liabilities as reported in Statement 1.11 in Finance Accounts 2019, € millions

Relevant Department and Nature of Liability	Amounts Outstanding
Finance	
ACP-EEC Convention of Lomé (contracts of Guarantee between State and European Investment Bank) Act, 1976	7.4
Strategic Banking Corporation of Ireland (SBCI)	508
Business, Enterprise and Innovation	
Credit Guarantee Act, 2012	5.2
Housing, Planning and Local Government	
Housing Finance Agency plc. (HFA)	4,488
Total	**5,009.2**

Source: Finance Accounts 2019[6]

2.2: Liabilities of public corporations

Public corporations are government-controlled entities, classified outside the general government sector due to their commercial activity. Public corporations are involved in both the financial sector (e.g. AIB, PTSB, VHI) and the non-financial sector (e.g. ESB, Dublin Airport Authority, An Post) of the economy.[7] As market units within the public sector, these entities do not contribute to the general government balance or debt. However, they play an important role in providing goods and services and, as such, there remains a possibility that, in the event of adverse economic challenges facing a public corporation, the government may decide to intervene. Accordingly, the liabilities of public corporations represent *potential* financial obligations for the government.

[6] https://www.gov.ie/en/publication/89166-finance-accounts-2019/

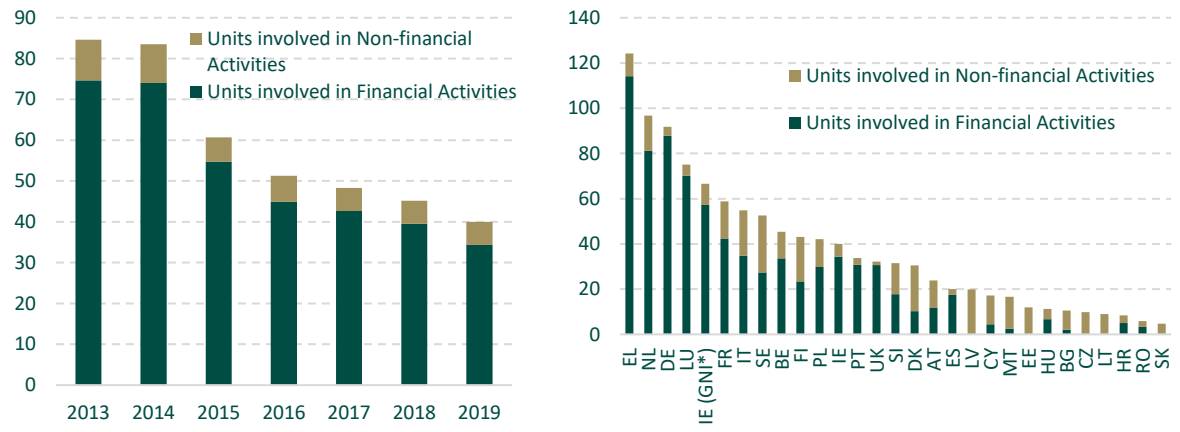
[7] A list of the bodies currently classified as public sector entities is published twice annually by the CSO. Available at:https://www.cso.ie/en/methods/governmentaccounts/classificationdecisions/registerofpublicsectorbodiesinireland/

The CSO has compiled data on the liabilities of public corporations annually since 2013, which they report to *Eurostat* on a confidential basis. These are defined as the stock of liabilities at year-end in the business accounts for each public corporation.

Figure 2a shows the estimated aggregate unconsolidated liabilities of these entities over the period 2013-2019. Only those entities whose liabilities exceed 0.01 per cent of GDP are included in this aggregate.[8] Liabilities of public corporations in Ireland declined sharply post 2013 due to deleveraging of both assets and liabilities by public financial corporations.

The level of liabilities of public corporations varies across the EU (figure 2b), where those member states with financial institutions (e.g. nationalised banks) under government control reporting a relatively higher level of liabilities. At end-2019, the liabilities of public corporations in Ireland was 66.6 per cent of GNI* (40 per cent of GDP), putting Ireland at the upper-end of the distribution, coming behind only Greece (124.3 per cent of GDP), the Netherlands (96.8 per cent of GDP), Germany (91.7 per cent of GDP) and Luxembourg (75.1 per cent of GDP).

Figure 2: Liabilities of public corporations a) Ireland; b) EU Member States 2019, per cent of GDP unless stated



Note: The UK is included in the graph as the data represents 2019 positions. 2018 values for France, Netherlands and Austria are included, as they currently have no reported values for 2019.
Underlying Irish data is provided in annex, table A.2.
Source: CSO and Eurostat.

Public banks and financial institutions are the main driver of these high levels of liabilities in public corporations – with the liabilities mainly consisting of deposits held in the public banks by households and other public and private entities. In general, financial institutions report high amounts of debt liabilities; crucially, however, they also hold significant assets, which are not captured in this analysis.

2.3: Off balance sheet Public Private Partnerships (PPPs)

A Public Private Partnership (PPP) is a long-term contractual arrangement between the public sector (a government body) and the private sector for the purpose of infrastructural development or services production. From a public policy perspective, entering into a PPP arrangement may lead to production in a more economically efficient manner. For instance, in the case of an infrastructure rollout, a PPP arrangement necessitates a smaller upfront impact on capital expenditure, as PPPs enable the distribution of the cost of capital infrastructure over a longer period. This provides increased flexibility – within government budget constraints – to provide a greater volume or quality of infrastructure in the short-term. Put another way, infrastructure delivery via PPPs offers the greater potential to increase

[8] The liabilities of the Central Bank of Ireland are excluded for the purpose of this analysis.

investment (by moving capital expenditure off the State's balance sheet) while reducing the risk exposure of the State's balance sheet.

Box 3: Off-balance sheet liabilities

The government's financial position depends on more than the assets and liabilities reported on the balance sheet – off-balance sheet liabilities have the capacity to result in unexpected fiscal consequences for the government. Such potential obligations facing the government may include future pension expenditure, demographic related costs, callable capital agreements and impending legal cases[9] – some of which are outlined below:

Pension obligations

Future pension and social insurance obligations of the government, while not recorded on the balance sheet, have the potential to result in significant future demands on government finances. These liabilities are not considered contingent liabilities. While the value of the pensions may be contingent for the recipients, as they are conditional on life expectancies, the aggregate pension and social security obligations facing the government can be estimated using known benefit formulas and demographic patterns.

As the largest off-balance sheet commitment of the government, accrued-to-date (ADL) pension liabilities are estimated to be €508.8bn or 256.1 per cent of GNI* at end-2018[10] - €359.2bn (180.8 per cent of GNI*) relates to social security pension schemes[11] and €149.6bn (75.3 per cent of GNI*) relates to defined benefit schemes for government employees.[12]

This signifies a sizable liability for the State. It represents the amount of money that would need to be set aside today to pay for all future social insurance pension payments arising from accrued benefits as at end-2018, along with all future expected superannuation benefit payments for public sector pensions of current and former staff arising from accrued service to end-2018.

Implicit Liabilities

The banking crisis, just over a decade ago, highlights the significant impact that implicit contingent liabilities can have on the government finances. Even in the absence of a contractual commitment, an implicit government obligation to maintain financial stability can ultimately translate into explicit contingent liabilities or even direct liabilities - resulting in a large financial burden for the State.[13]

Implicit liabilities extend beyond the financial sector to incorporate welfare obligations and aging costs. As the demographics of a country evolves, additional expenditure pressure can be placed on public services, such as pension, education, welfare and health systems. Most recent forecasts, as outlined by the Department, project an increase in age-related expenditure of 6.5 percentage points of GNI* by 2070 - with expenditure demands peaking in 2059 at 31.2 per cent of GNI*, before falling to 30.3 per cent of GNI* in 2070.[14]

Callable capital in International Financial Institutions

The government subscribes capital to International Financial Institutions (IFIs) – generally Multilateral Development Banks (MDBs) – to enable these institutions to provide financing and to leverage off international financial markets. Subscribed capital consists of both payable capital and callable capital.

Callable capital is a commitment of the government to provide a specified amount at a future date if the IFI needs it to do so – the callable capital is unlikely to be requested – thus representing a contingent liability. Ireland's potential liability relating to callable capital is approximately 5.95 per cent of GNI*. See table A.3 in the Annex for more detail.

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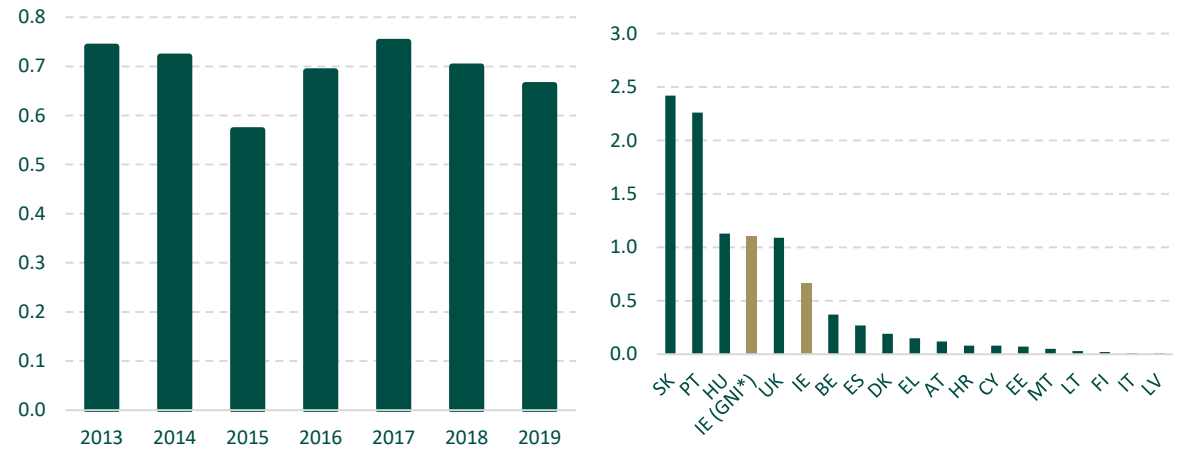
[9] The State Claim Agency's estimated outstanding liability at year-end 2019 is €3.63bn in respect of their claims portfolio at end-2019. https://www.ntma.ie/annualreport2019/downloads/8953-NTMA-Annual-Report-2019-State-Claims-Agency.pdf
[10] https://www.cso.ie/en/releasesandpublications/ep/p-eipl/estimatesofirishpensionliabilities2018/bgn/
[11] https://www.gov.ie/en/publication/e1233-accrued-to-date-liability-social-security-pension-schemes/
[12] https://www.gov.ie/en/publication/70acca-actuarial-review-of-public-service-pension-liabilities/
[13] Since 2010, a number of significant reforms were introduced, aimed at strengthening the resilience of the banking sector in order to build capacity to absorb economic shocks, while ensuring that banks continue to finance economic activity and growth. The introduction of these reforms reduce the risk of the banking sector needing government support in the future.
[14] https://www.gov.ie/en/publication/2e8463-population-ageing-and-the-public-finances/

In Ireland, significant infrastructure projects have been delivered on behalf of the State through the use of PPP procurement – the largest investments in PPPs are in the transport sector (productive infrastructure) and the education sector (social infrastructure), with other areas of PPP investment in the justice, health and housing sectors. The procurement of PPP projects played a significant role in facilitating the delivery of important infrastructure projects, in response to the fiscal crisis. Procurement by PPP enabled the implementation and development of infrastructure projects when the Exchequer was seriously constrained in terms of its ability to fund infrastructure directly.

Engaging in PPP agreements can be a useful policy tool – promoting an increased investment in public infrastructure while having a limited impact on the government finances. A prudent fiscal sustainability analysis should include a continued examination of existing and new PPP agreements to ensure objectives are achieved and any *potential* risk on the long-term budget flexibility is kept to a minimum.

Figure 3: Off-balance sheet PPPs a) Ireland; b) EU Member States 2019, per cent of GDP unless stated



Note: The liabilities reported in these graphs relate to long-term construction PPP contracts for which the assets are recorded outside the government accounts. The UK is included in the graph as the data represents 2019 positions. Bulgaria, Czechia, Germany, France, Luxembourg, Netherlands, Poland, Romania, Slovenia and Sweden reported no contingent liabilities related to on-going PPP contracts for 2019.
Underlying Irish data is provided in annex, table A.4.
Source: CSO and Eurostat.

The CSO reports data on PPPs to Eurostat as part of the bi-annual EDP notification and publishes these data items in conjunction with the Government Finance Statistics annual results.[15] Figure 3a shows the 'adjusted capital value' of off-balance sheet PPP contracts – this reflects the current value of the asset at the time of reporting and can be described as the outstanding debt (or liability) associated with ongoing PPP contracts. This differs from the reporting under the CSO's EDP notification, which requires the recording of the initial contractual capital value along with other details, such as the unitary and other payments made under the PPP contract.

At year-end 2019, Ireland's adjusted capital value of off-balance sheet PPPs was 0.7 per cent of GDP or 1.1 per cent of GNI*.

In terms of EU comparison, no EU Member State has off-balance public-private partnerships liabilities in excess of 2.5 per cent of GDP; by far the most significant were in Slovakia and Portugal at 2.4 and 2.3 per cent, respectively. Ireland's level of off-balance sheet liabilities relating to PPP contracts, at 1.1 per cent of GNI*, is higher than most other member states, but when measured in terms of GDP Ireland is closer to the EU average.

[15] https://www.cso.ie/en/statistics/governmentaccounts/governmentfinancestatisticsa/

2.4: Non-performing loans

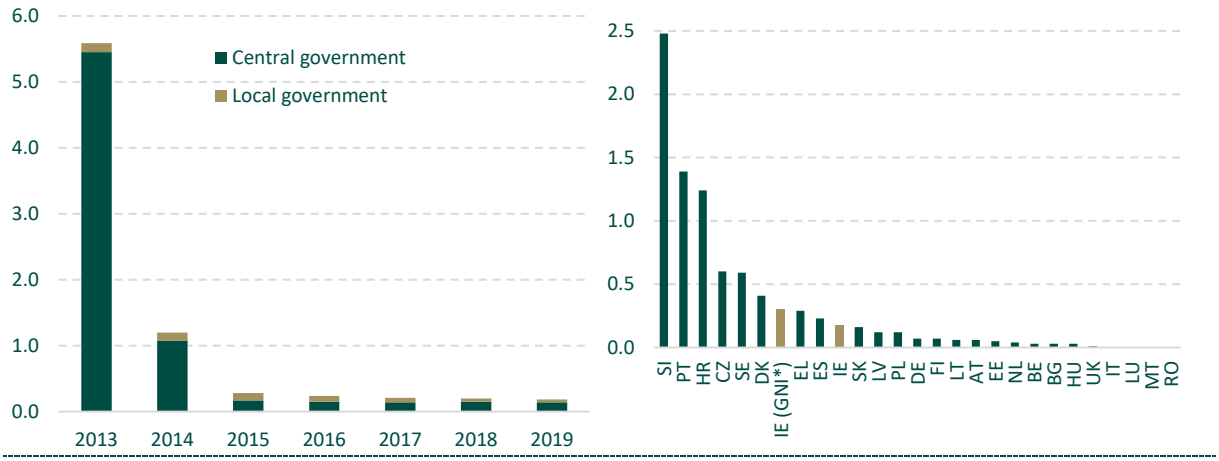
A loan is non-performing if it satisfies all or some of the following criteria:

- payments of the principle and/or interest are more than 90 days past due;
- interest payments equal to 90 days or more have been capitalised, refinanced, or delayed by agreement;
- payments are less than 90 days overdue, but there are other good reasons (such as a debtor filing for bankruptcy) to doubt that payments will be made in full.

As non-performing loans are a government asset, rather than a liability, recognised on the government's balance sheet, they do not meet the definition of a contingent liability. However, uncertainty around their repayment implies a potential loss for the government – so the financial risk they impose should not be underestimated.

Figure 4a shows the estimated value of non-performing loans of government over the period 2013-2019. The data are based on a survey covering the local government section of the Department of Housing, Local Government and Heritage and central government bodies identified as holding loan assets.

Figure 4: Non-performing loans of government a) Ireland; b) EU Member States 2019, per cent of GDP unless stated



Note: The UK is included in the graph as the data represents 2019 positions. Cyprus is excluded for presentation purposes – Cyprus peaked as the Member State with the largest stock of non-performing loan as 32.4 per cent of GDP in 2018. This drastic increase was a consequence of a large transaction that resulted in the transfer of non-performing loans from a public financial corporation (classified outside government) to a government unit. Cyprus' stock of non-performing loans in 2019 was 28.8 per cent of GDP. Data is currently not available for France. Underlying Irish data is provided in annex, table A.5.
Source: Department of Finance calculations and Eurostat.

The value of non-performing loans held by the Irish central and local government was €0.7bn (0.2 per cent of GDP) in 2019, a drastic fall from the 2013 high watermark of €10.1bn (5.6 per cent of GDP). This decrease is largely a result of the Special Liquidation of IBRC in February 2013, after which loans with a par value of €21.7bn were prepared, brought to the market and sold, a process which ultimately resulted in a reduction in the value of non-performing loans on the general government balance sheet.

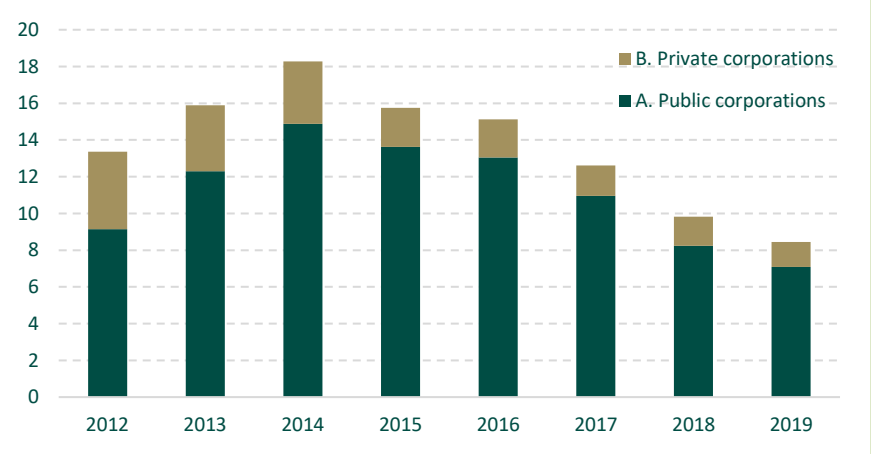
Figure 4b puts Irish developments in a European context. The majority of member states recorded a share of non-performing loans of government of less than 1 per cent of GDP; the exceptions were Slovenia (2.5 per cent), Portugal (1.4 per cent), and Croatia (1.2 per cent). Once again, the Irish figure – at below 0.5 per cent in terms of both GDP and GNI* – was broadly in line with the EU norm.

Box 4: Participation of government in the capital of corporations

Council Directive 2011/85 of 8th November 2011 requires the publication of data *on "the participation of general government in the capital of private and public corporations"*. While such equity investments do not fall into the category of contingent liabilities, they do have a potential to affect the financial position of the government in both a positive and negative way – through a return on equity.

The participation of government in the capital of corporations is defined as the value of the equity held by the government in public and private enterprises. These holdings are government assets and represent the property rights of government on corporation capital, entitling the holders to a share on corporation profit and on the net worth of the corporation in the event of liquidation.

Figure 5: Participation of the Irish government in the capital of corporations, per cent of GDP



Note: Underlying Irish data is provided in annex, table A.6.
Source: CSO

Figure 5 shows evolution of these capital holdings over the period 2012 – 2019. The capital investment is subdivided into holdings of shares and other equity in public corporations and private corporations. These values are based on the annual reports of commercial and non-commercial semi-state corporations and on data extracted from the ISIF annual report.

The government's equity investment in public corporations was 11.8 per cent of GNI* (7.1 per cent of GDP) and private corporations was 2.3 per cent of GNI* (1.4 per cent of GDP) at end-2019.

2.5: An insight into contingent liabilities - responding to the Covid-19 pandemic

As mentioned in section 2.1, government guarantees have played an integral part in the policy response to the Covid-19 pandemic, both in Ireland and across other global economies. Although finalised data for 2020 is not currently available, this section aims to provide an estimate of the forecasted value of contingent liabilities that may result from guarantees provided in a response to the Covid-19 pandemic.

With an aim of mitigating the impact of the pandemic on the economy, Ireland introduced two State guarantees, the Covid-19 Credit Guarantee Scheme (CGS)[16] and the State guarantees for credit notes issued by Irish travel agents and tour operators, as outlined in the *Budget 2021 Economic and Fiscal Outlook*[17].

The larger of these two – the Covid-19 CGS: is a €2bn scheme to facilitate lending to eligible businesses who are facing liquidity challenges due to the pandemic. An 80 per cent State guarantee is provided on

[16] The *Credit Guarantee (Amendment) Act 2020* amends the *Credit Guarantee Act 2012* as necessary to provide for the establishment of the Scheme. More information on the Scheme available at: https://enterprise.gov.ie/en/What-We-Do/Supports-for-SMEs/Access-to-Finance/SME-Credit-Guarantee-Scheme/
[17] http://budget.gov.ie/Budgets/2021/Documents/Budget/Budget%202021_Economic%20and%20Fiscal%20Outlook.pdf

loans – creating an incentive for banks to lend under this scheme. Conditional on full uptake, this scheme is estimated to result in a maximum contingent liability of €1.6 billion (0.79 per cent of GNI*).

Coupled with these national schemes, the government extended guarantees necessary to participate in instruments developed at the European level in response to the pandemic.[18]

These include a guarantee of €483 million or 0.24 per cent of GNI*, to counter-guarantee the risk being borne by the Union in offering the *European instrument for temporary Support to mitigate Unemployment Risks in an Emergency* (SURE). The SURE scheme aims to provide financial assistance in the form of loans, from the EU to affected member states, to address sudden increases in public expenditure relating to the preservation of employment. Ireland will be availing of a loan to the value of €2.5 billion under this scheme to assist in covering expenditure on the Temporary Covid-19 Wage Subsidy Scheme.[19]

Ireland is also participating in the *European Investment Banks Pan-European Guarantee Fund* (PEGF), which aims to respond to the economic impact of the Covid-19 pandemic by ensuring that companies, in participating member states, have sufficient short-term liquidity available. The contingent liability, to cover any *potential* losses on the fund, is capped for Ireland at €164.7 million or 0.08 per cent of GNI*.

Figure 6: Comparison of a) above the line; b) below the line measures announced in response to Covid-19 pandemic, per cent of GDP unless stated

Note: The country level information available in the dataset varies depending on country-specific circumstances. The estimates are preliminary, as governments continue to announce additional measures and/or finalise the details of individual measures already announced. The implementation of the measures could span across 2020, 2021, or beyond. Values are based on GDP measures outlined in the January 2021 World Economic Outlook.[20]
Source: International Monetary Fund, *Fiscal Monitor Database of Country Fiscal Measures in Response to the COVID-19 Pandemic*[21]; IE values are based on Department of Finance calculations

Figure 6 provides a preliminary insight into the key fiscal measures governments have announced, or implemented in selected economies, in response to the Covid-19 pandemic. The range of instruments applied across countries in their attempts to counteract the impact of Covid-19 on their respective

[18] The EU budget gives rise to certain contingent liabilities for member states, the most significant of which is the Next Generation EU (NGEU) Recovery Instrument, which provides for the EU to borrow on capital markets, with this borrowing guaranteed by member states. The Recovery and Resilience Facility (RRF) will be the prominent programme funded by NGEU. The maximum contingent liability for the Irish State annually amounts to Ireland's proportionate share of up to 2% of EU GNI (Once the amended Own Resources Decision is in place), but for this contingent liability to be realised would involve member states failing to meet all of their obligations, which is an extreme assumption.
[19] https://ec.europa.eu/ireland/news/commission-proposes-to-provide-2.5-billion-euro-to-ireland-under-sure_en
[20] https://www.imf.org/en/Publications/FM/Issues/2021/01/20/fiscal-monitor-update-january-2021
[21] https://www.imf.org/en/Topics/imf-and-covid19/Fiscal-Policies-Database-in-Response-to-COVID-19

economies is vast. In the case of Ireland, direct supports have played the most prominent role in this response[22].

Section 3: Conclusion

Analysis in this paper shows that contingent liabilities (as reported under Council Directive 2011/85) have fallen sharply – from 157.3 per cent of GNI* (122.2 per cent of GDP) in 2013 to 68 per cent of GNI* (40.9 per cent of GDP) at end-2019. This decrease is driven predominantly by the reduction in government guarantees extended to the financial sector and the de-leveraging of public sector financial corporations. Ireland compares favourably by EU standards, trending at or below the EU norm in terms of the contingent liabilities.

Table 3: Contingent Liabilities and non-performing loans (reported under Council Directive 2011/85), per cent of GNI*

	2013	2019
Total	**157.3**	**68.0**
Total stock of guarantees	*40.9*	*0.0*
Outstanding liabilities of government controlled entities classified outside GG sector	*108.1*	*66.6*
Off-balance sheet PPPs of general government	*1.0*	*1.1*
Non-performing loans	*7.4*	*0.3*

Source: CSO, Department of Finance calculations

These trends signal a reduction in the risks to the actual public sector balance sheet – however, it must be remembered that contingent liabilities can be an important way of achieving policy objectives. In this context, these contingent liabilities are likely to have increased since the pandemic given that *inter alia* guarantees have been an important policy response

While explicit contingent liabilities of the government can facilitate policy objectives, they also generate potential risks to the stability of government finances. Equally important are implicit future liabilities – Ireland's accrued-to-date pension obligations are estimated at 256.1 per cent of GNI* (155.6 per cent of GDP) at end-2018, while in addition to this, Ireland's age-related implicit liabilities are forecast to grow by 6.5 per cent of GNI* to a value equal to 30.3 per cent of GNI* in 2070.

The level of contingent liabilities in Ireland and across global economies is likely to increase in the aftermath of the Covid-19 pandemic. On this basis, the continued reporting and monitoring of these forms of liabilities is crucial from a sustainability and policy perspective – to facilitate this the Department will continue to publish data on contingent liabilities.

[22] For further information please see the Department of Finance's 'Taking Stock: The Fiscal Response to Covid-19": https://www.gov.ie/en/publication/84a0c-taking-stock-the-fiscal-response-to-covid-19/

Annex

Figure A.1: Type of Liabilities

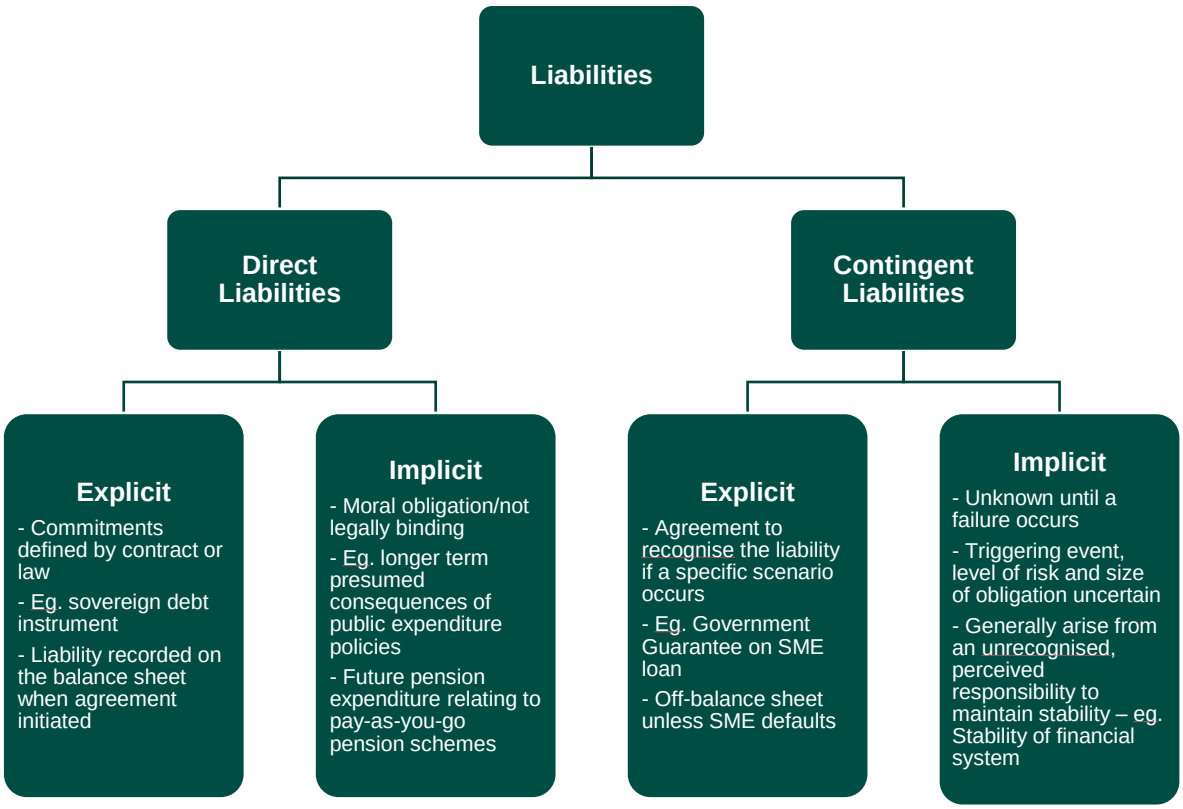


Table A.1: Outstanding amount of guarantees, per cent of GDP

	2010	2011	2012	2013	2014	2015	2016	2017	2018	2019
GENERAL GOVERNMENT										
One-off guarantees										
Total stock of guarantees, excluding debt assumed by government	96.0	79.8	65.8	31.1	12.9	4.3	1.5	0.1	0.0	0.0
of which: public corporations	42.3	38.0	35.3	8.4	3.8	1.0	0.5	0.1	0.0	0.0
Memo item: financial corporations	*96.0*	*79.8*	*65.8*	*31.1*	12.9	4.3	1.5	*0.1*	*0.0*	*0.0*
Memo item: guarantees given in the context of financial turmoil	*95.2*	*79.8*	*65.1*	*30.3*	12.3	4.3	1.5	*0.1*	*0.0*	*0.0*
Standardised guarantees										
Total stock of government guarantees	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
CENTRAL GOVERNMENT										
One-off guarantees										
Total stock of guarantees, excluding debt assumed by government	96.0	79.8	65.8	31.1	12.9	4.3	1.5	0.1	0.0	0.0
of which: public corporations	42.3	38.0	35.3	8.4	3.8	1.0	0.5	0.1	0.0	0.0
Memo item: financial corporations	*96.0*	*79.8*	*65.8*	*31.1*	12.9	4.3	1.5	*0.1*	*0.0*	*0.0*
Memo item: guarantees given in the context of financial turmoil	*95.2*	*79.8*	*65.1*	*30.3*	12.3	4.3	1.5	*0.1*	*0.0*	*0.0*
Standardised guarantees										
Total stock of government guarantees	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
STATE GOVERNMENT										
One-off guarantees										
Total stock of guarantees, excluding debt assumed by government	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.
of which: public corporations	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.
Memo item: financial corporations	*n.a.*	*n.a.*	*n.a.*	*n.a.*	*n.a.*	*n.a.*	*n.a.*	*n.a.*	*n.a.*	*n.a.*
Memo item: guarantees given in the context of financial turmoil	*n.a.*	*n.a.*	*n.a.*	*n.a.*	*n.a.*	*n.a.*	*n.a.*	*n.a.*	*n.a.*	*n.a.*
Standardised guarantees										
Total stock of government guarantees	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.
LOCAL GOVERNMENT										
One-off guarantees										
Total stock of guarantees, excluding debt assumed by government	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
of which: public corporations	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Memo item: financial corporations	*0.0*	*0.0*	*0.0*	*0.0*	*0.0*	*0.0*	*0.0*	*0.0*	*0.0*	*0.0*
Memo item: guarantees given in the context of financial turmoil	*0.0*	*0.0*	*0.0*	*0.0*	*0.0*	*0.0*	*0.0*	*0.0*	*0.0*	*0.0*
Standardised guarantees										
Total stock of government guarantees	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0

Source: CSO

Table A.2: Liabilities of public corporations, per cent of GDP

	2013	2014	2015	2016	2017	2018	2019
GENERAL GOVERNMENT							
Outstanding liabilities of government controlled entities classified outside GG sector	84.6	83.5	60.7	51.3	48.3	45.1	40.0
of which:							
Liabilities of units involved in financial activities	74.6	74.0	54.7	44.9	42.7	39.5	34.4
Liabilities of units involved in other activities	10.0	9.5	6.0	6.3	5.7	5.6	5.6
Of which: loss-making non-financial units	1.7	0.8	0.2	0.7	0.6	0.7	1.1
CENTRAL GOVERNMENT							
Outstanding liabilities of government controlled entities classified outside GG sector	84.6	83.5	60.7	51.3	48.3	45.1	40.0
of which:							
Liabilities of units involved in financial activities	74.6	74.0	54.7	44.9	42.7	39.5	34.4
Liabilities of units involved in other activities	10.0	9.5	6.0	6.3	5.7	5.6	5.6
Of which: loss-making non-financial units	1.7	0.8	0.2	0.7	0.6	0.7	1.1
STATE GOVERNMENT							
Outstanding liabilities of government controlled entities classified outside GG sector	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a
of which:							
Liabilities of units involved in financial activities	*n.a.*	*n.a.*	*n.a.*	*n.a.*	*n.a.*	*n.a.*	n.a
Liabilities of units involved in other activities	*n.a.*	*n.a.*	*n.a.*	*n.a.*	*n.a.*	*n.a.*	n.a
Of which: loss-making non-financial units	*n.a.*	*n.a.*	*n.a.*	*n.a.*	*n.a.*	*n.a.*	n.a
LOCAL GOVERNMENT							
Outstanding liabilities of government controlled entities classified outside GG sector	-	-	-	-	-	-	-
of which:							
Liabilities of units involved in financial activities	-	-	-	-	-	-	-
Liabilities of units involved in other activities	-	-	-	-	-	-	-
Of which: loss-making non-financial units	-	-	-	-	-	-	-

Source: CSO

Table A.3: Callable capital in International Financial Institutions

International Institutions	Callable Capital, %GNI*	Callable Capital, % GDP
European Stability Mechanism (ESM) [23]	4.62	2.77
European Investment Bank (EIB)[24]	0.70	0.42
International Bank for Reconstruction and Development (IBRD)[25]	0.38	0.23
Other International Organisations[26]	0.25	0.15

Source: Department of Finance calculations

[23] https://www.esm.europa.eu/sites/default/files/esm-annual-report-2019.pdf
[24] https://www.eib.org/attachments/general/reports/eib_financial_report_2019_en.pdf
[25] http://pubdocs.worldbank.org/en/521601597072122154/IBRDFinancialStatementsJune2020.pdf
[26] Includes the European Bank for Reconstruction and Development (EBRD), Council of Europe Development Bank (CEDB), Asian Development Bank, Asian Infrastructure Investment Bank (AIIB), the African Development Bank (AfDB) and the Multilateral Investment Guarantee Agency (MIGA).

Table A.4: Off-balance sheet PPPs, per cent of GDP

	2013	2014	2015	2016	2017	2018	2019
Total general government	0.7	0.7	0.6	0.7	0.7	0.7	0.7
of which by government subsectors							
Central government	0.7	0.7	0.6	0.7	0.7	0.7	0.7
State government	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.
Local government	0	0	0	0	0	0	0
Social security funds	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.

Source: CSO

Table A.5: Non-performing loans, per cent of GDP[27]

	2013	2014	2015	2016	2017	2018	2019
Total general government	5.6	1.2	0.3	0.2	0.2	0.2	0.2
of which by government subsectors							
Central government	5.5	1.1	0.2	0.2	0.1	0.2	0.1
State government	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.
Local government	0.1	0.1	0.1	0.1	0.1	0.1	0.0
Social security funds	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.

Source: Department of Finance calculations

Table A.6: Participation of government in the capital of corporations, per cent of GDP

	2012	2013	2014	2015	2016	2017	2018	2019
A. Public corporations	9.1	12.3	14.9	13.6	13.0	10.9	8.2	7.1
B. Private corporations	4.2	3.6	3.4	2.1	2.1	1.7	1.6	1.4

Source: CSO

[27] The central government amount for non-performing loans is reported in this table as a gross figure, while the quarterly financial accounts of general government reported to Eurostat and published nationally by the CSO refer to an asset position net of provisions for impairment.

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